

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**Office of Audit Services
Region IX**

**SUTTER OAKS - ARDEN AND SUTTER
OAKS - CARMICHAEL SKILLED NURSING
FACILITY BILLINGS AND COSTS FOR
ANCILLARY MEDICAL SUPPLIES FOR
THE PERIOD JANUARY 1, 1994
THROUGH DECEMBER 31, 1995**

The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed as well as other conclusions and recommendations in this report represent the findings and opinions of the HHS/OIG/OAS. Final determination on these matters will be made by authorized officials of the HHS operating divisions.



JUNE GIBBS BROWN
Inspector General

MARCH 1998
A-09-98-00073



Region IX
Office of Audit Services
50 United Nations Plaza
San Francisco, CA 94102

MAR 24 1993

CIN: A-09-98-00073

Ms. Jacqueline Anderson
General Manager
Medicare Program
Blue Cross of California
P.O. Box 9140
Oxnard, California 93031-9140

Dear Ms. Anderson:

This final report provides you with the results of an Office of Inspector General (OIG) audit of Sutter Health's (Sutter) billings to Medicare for ancillary medical supplies and its associated costs as claimed on the Medicare cost reports for Sutter Oaks Nursing Center-Carmichael and Sutter Oaks Nursing Center-Arden for the calendar years ended (CYE) December 31, 1994 and December 31, 1995.

During this 2-year period, Sutter billed Medicare a total of \$1,157,930 for these two skilled nursing facilities (SNFs) for items identified as ancillary medical supplies (i.e., medical supplies not included in the patient's daily routine care) and claimed costs of \$747,801 for these items.

The objective of our review was to determine if unallowable charges had been billed to Medicare and if inappropriate costs had been claimed on the cost reports for ancillary medical supplies.

According to Medicare reimbursement rules, items and services that can be considered ancillary are limited to only those items and services that are directly identifiable to an individual patient, furnished at the direction of a physician because of special medical needs, and are either not reusable, represent a cost for each preparation, or are complex medical equipment.

Our audit of a judgement sample of 1,031 items billed to Medicare as ancillary medical supplies showed that 74 items, or about 7 percent, were actually routine medical supplies. In addition, our judgement sample of the costs for 191 items classified as ancillary medical supplies showed that 74 of the items, or about 39 percent, were routine. We did not quantify the full impact of the billing errors and misclassified costs as our review was

limited to determining what types of items and services were classified as ancillary and were inappropriate as such.

Sutter also incorrectly classified 18 of its 28 supply accounts, for a net amount of \$282,018, on the 4 cost reports we reviewed. The classification errors resulted in excessive ancillary costs. Mutual of Omaha (Mutual), Sutter's fiscal intermediary (FI) during the audit period, had previously identified the same problem on prior audits and notified Sutter officials.

The improper billings and cost classifications occurred because Sutter had not adequately maintained its master list (including the current version used at the time of our review) that classified each medical supply item as routine or ancillary according to Medicare's rules.

The accounts were incorrectly classified because Sutter had not followed its written procedures that required it to take into account any problems identified by its FI in the prior years' Medicare audits. Instead, Sutter's accounting staff said that they treated these accounts consistent with the cost reports that were prepared in the prior years. They believed at the time that their method was appropriate and would not result in overpayments from Medicare. Sutter's staff also said that due to the sudden death of the employee responsible for preparation of the CYE 1994 cost reports, the reports in the following year had to be completed by other employees.

Sutter elected to change its FI from Mutual to Blue Cross of California (Blue Cross) effective January 1, 1998. Therefore, in a separate report to Mutual (CIN: A-09-97-00075), we recommended that it ensure that Sutter determines the fiscal impact of our findings and makes an appropriate refund to Medicare for the periods before January 1, 1998. In this report, we recommend that Blue Cross ensure that Sutter:

- ▶ Reviews its master list of medical supplies to identify and correct all of its classifications of routine medical supplies that are classified as ancillary,
- ▶ Does not bill future routine items as ancillary or claim routine costs as ancillary, and
- ▶ Provides training to its staff to ensure that accounts are accurately classified and takes steps to ensure that its written procedures are consistently followed.

In its response to our draft report, Sutter agreed with our recommendations. Sutter also listed corrective actions it has taken or soon will take.

Mutual indicated in its response to our draft that it would take steps to implement our recommendations for claims prior to January 1, 1998. Blue Cross verbally concurred with the recommendations in our draft that related to periods beginning with January 1, 1998. Sutter's and Mutual's responses are attached as appendices.

INTRODUCTION

Background

As part of the Department of Health and Human Services' efforts to combat fraud, waste, and abuse, the OIG, in partnership with the Health Care Financing Administration (HCFA) and the Administration on Aging, undertook an initiative called Operation Restore Trust. This project was designed to specifically target Medicare and Medicaid abuse and misuse in nursing home care, home health care, and durable medical equipment, three of the fastest growing areas in Medicare.

The OIG's audit of Sutter was one of several conducted in a national review of ancillary medical supplies. States included in this review were California, Florida, Illinois, New York, and Texas. As part of this national review, we identified those SNFs with significantly higher medical supply costs than comparable SNFs. However, we selected Sutter for this review because we wanted to examine at least one facility whose ancillary medical supply costs were not excessive when compared with other SNFs of similar size in California.

Sutter is a multi-provider, integrated health care delivery system headquartered in Sacramento, California. One Sutter affiliate owned four nursing facilities (three are freestanding and one is a distinct part) and a second affiliate owned another distinct part skilled nursing facility. Sutter prepared the cost reports and provided other financial and accounting services to all five of these facilities.

This report provides the results of our audit of two of its five SNFs, Sutter Oaks Nursing Center-Carmichael (Carmichael) and Sutter Oaks Nursing Center-Arden (Arden). Mutual served as the FI for the two SNFs included in this report.

Another two SNFs, also handled by Mutual (Sutter Oaks Alzheimers Center and Sutter Amador), did not have significant Medicare costs and were not included in our audit. Blue Cross served as the FI for the remaining SNF, a hospital-based facility named Sutter Transitional Care Center - Sutter Oaks Nursing Center-Midtown. The results of our audit of that SNF will be reported to Blue Cross in a separate report.

Medicare generally reimburses SNFs on a reasonable cost basis as determined under principles established in the law and regulations. In order to determine their reasonable costs, providers are required to submit cost reports annually, with the reporting period based on the provider's fiscal accounting year. The SNFs are paid on an interim basis (based upon their billings to Medicare), and the cost report is used to arrive at a final settlement. Costs are classified on the cost report as either routine or ancillary.

Routine services are generally those services included by the provider in a daily service--sometimes referred to as the "room and board" charge. Included in routine services are the regular room, dietary and nursing services, minor medical and surgical supplies, and the use of certain equipment and facilities for which a separate charge is not customarily made.

According to Medicare rules, "... the following types of items and services. . . are always considered routine in an SNF for purposes of Medicare cost apportionment, even if customarily considered ancillary by an SNF:

- " 0 All general nursing services, including administration of oxygen and related medications. . . handfeeding, incontinency care, tray service, enemas, etc.

- " 0 Items which are furnished routinely and relatively uniformly to all patients, e.g., patient gowns, paper tissues, water pitchers, basins, bed pans, deodorants, mouthwashes.

- " 0 Items stocked at nursing stations or on the floor in gross supply and distributed or utilized individually in small quantities, e.g., alcohol, applicators, cotton balls, bandaids, antacid, aspirin, (and other nonlegend drugs ordinarily kept on hand), suppositories, tongue depressors.

"0 Items which are utilized by individual patients but which are reuseable and expected to be available in an institution providing an SNF level of care, e.g., ice bags, bed rails, canes, crutches, walkers, wheelchairs, traction equipment, other durable medical equipment (DME) which does not meet the criteria for ancillary services in SNFs under 52203.2, and the requirements for recognition of ancillary charges under §2203....

"0 Special dietary supplements used for tube feeding or oral feeding, such as elemental high nitrogen diet, even if written as a prescription item by a physician, because these supplements have been classified by the Food and Drug Administration as a food rather than a drug." (Provider Reimbursement Manual, section 2203.1)

The Medicare rules further specify the treatment of special dietary supplements as follows:

"Enteral nutrients provided during a stay that is covered by Part A are classified as food and included in the routine Part A payment sent to the SNF."
(Intermediary Manual, section 3660.6A)

Ancillary services are those services directly identifiable to individual patients, such as laboratory, radiology, drugs, medical supplies, and therapies. Section 2203.2 of the Provider Reimbursement Manual, effective for most of our audit period,¹ specified that certain items and services could be considered ancillary if they met each of the following three requirements:

"0 direct identifiable services to individual patients, and

"0 furnished at the direction of a physician because of specific medical needs, and

"0 one of the following:

- Not reusable - e.g., artificial limbs and organs, braces, intravenous fluids or

¹ This section was revised effective March 1995. The phrase "furnished at the direction of a physician because of specific medical needs" (see above) was replaced by "Not generally furnished to most patients."

solutions, oxygen (including medications), disposable catheters;

- Represent a cost for each preparation, e.g., catheters and related equipment, colostomy bags, drainage equipment, trays and tubing; or

- Complex medical equipment - e.g., ventilators, intermittent positive pressure breathing (IPPB) machines, nebulizers, suction pumps, continuous positive airway pressure (CPAP) devices, and bead beds such as air fluidized beds."

Medicare pays its portion of a provider's reasonable costs based upon an apportionment between program beneficiaries and other patients so that Medicare's share of the costs is based on services received by Medicare beneficiaries. For routine costs, Medicare's share is determined on the basis of a ratio of Medicare patient days to total patient days. For ancillary costs, Medicare's share is determined on the basis of the ratio of total covered beneficiary charges for ancillary services to total patient charges for such services.

Classifying costs as ancillary rather than as routine can result in higher Medicare reimbursement to SNFs because of two factors. First; SNFs generally have higher Medicare utilization for ancillary services than for routine services. That is, Medicare eligible patients generally receive more ancillary services than other patients but comprise a smaller portion of the total number of patients. Thus, Medicare's share of ancillary costs is usually greater than its share of routine costs. Second, Federal law (specifically, section 1888 of the Social Security Act) limits Medicare reimbursement for SNFs' routine costs to 112 percent of the mean operating costs of other similar SNFs. Thus, Medicare does not share in routine costs exceeding the Federal limit, unless the provider applies for and receives an exception from HCFA.

The HCFA administers the Medicare program and designates certain FIs to perform various functions, such as processing Medicare claims, performing audits, and providing consultative services to assist SNFs as providers.

Objective, Scope and Methodology

Our objective was to determine if unallowable charges had been billed to Medicare and whether costs had been misclassified on the Medicare cost reports as ancillary medical supplies for the 2-year period ended December 31, 1995.

According to its final cost reports, Sutter billed Medicare \$620,802 for ancillary medical supplies for CYE December 31, 1994 and \$537,128 for CYE December 31, 1995 (a total of \$1,157,930). It claimed \$469,927 as costs for these supplies for CYE December 31, 1994 and \$277,874 for CYE December 31, 1995 (a total of \$747,801).

To accomplish our objective, we reviewed a judgmental sample of 1,031 medical supply line items billed to Medicare as ancillary medical supplies (totaling \$18,955) and discussed billing procedures with Sutter's staff. To select our billings, we selected a judgmental sample of Medicare patients and then reviewed all charges to Medicare for those patients.

In addition, we gained an understanding of Sutter's accounting system, reconciled the amounts claimed on the Medicare cost reports for ancillary medical supplies to the accounting records, and examined a judgmental sample of 191 ancillary medical supply line items that were classified as ancillary costs (totaling \$24,269). For our judgmental sample of 191 line items, we selected invoices of those vendors that appeared to us to account for the most costs in each account.

Since Sutter classified medical supplies according to its master list, we reviewed the current master list, dated April 9, 1997, to determine if it contained routine items that were classified as ancillary medical supplies.

We relied on the FI's medical review staff to determine whether the sampled items were properly classified as ancillary using Medicare's guidelines. Because our samples were not random, we cannot project the results of our sample to the total billings or costs claimed.

Our review was made in accordance with generally accepted government auditing standards. The field work was performed at Sutter's offices in Sacramento, California during March through October of 1997.

FINDINGS AND RECOMMENDATIONS

We found that routine medical supplies were billed to Medicare as ancillary supplies. Of the 1,031 line items billed as ancillary medical supplies that we examined, we found that 74, or about 7 percent, were actually routine medical supplies and should not have been billed to Medicare as ancillary. The inappropriate billings totaled \$1,107, or about 6 percent of the total amount we examined (\$18,955).

The routine items that we identified as being billed as ancillary were applicators, Formula Fiber and Isosource (both food supplements), Geo mattress pads (a reusable mattress pad), and Driflo underpads (for incontinent care).

In addition to the improper billings, we found that costs for routine medical supplies were misclassified as ancillary on the Medicare cost reports. Of the 191 line items of ancillary medical supply costs that we examined, we found that 74 items, or about 39 percent, were actually routine medical supplies and should not have been included as ancillary costs. The inappropriate costs totaled \$8,980, or about 37 percent of the total amount we examined (\$24,269).

The improper ancillary costs included the following routine items:

Adult briefs	Medicine cup
Applicator (6 inch)	Miscellaneous supplies
Attends brief liners	Mouthwash
Basin, emesis	Ora-swab brush
Cartridge, dry ink-black comb	Paper (20#)
Deodorant	Shave cream
Driflo underpads	Straw (flex 7-3/4 wrap)
Facial tissue	Tape, video VHS
Formula Fibersource	Thermometer cleaner
Formula Glucerna	Thermometer probe cover
Geo mattress pads	Toothbrush
Hydrogen peroxide	Toothpaste
Isosource	Twin blade razor
Liner (24x23 .4 ml)	Urinal (36 ounce)
Lotion, soft conditioner	Washcloth, disposable
	Water cup

Because our samples were not chosen in a random manner, the results we noted may not necessarily be representative of the total ancillary billings or costs included as ancillary on the cost reports.

Sutter also incorrectly classified 18 out of 28 of its medical supply accounts on the 4 cost reports we reviewed for CYE December 31, 1994 and December 31, 1995. Five of the 18 incorrectly classified accounts (totaling \$152,988) were reclassified as ancillary medical supplies but should have been reclassified to routine cost centers.

The remaining 13 of the 18 incorrectly classified accounts were left in central supplies. The central supply costs were then allocated entirely to ancillary medical supplies for CYE December 31, 1994 and allocated for the most part (86 percent for Carmichael and 66 percent for Arden) to ancillary medical supplies for CYE December 31, 1995. Of the 13 accounts, 4 accounts (totaling \$137,734) should have been transferred to ancillary medical supplies. The other 9 accounts (totaling \$266,764) should have been transferred to various routine cost centers. As a result of the incorrect classifications of the 18 accounts, ancillary medical supply costs were overstated by \$282,018 (\$152,988 less \$137,734 plus \$266,764).

The FI identified the problem with the incorrectly classified accounts on Sutter's CYE December 31, 1991 and December 31, 1992 cost reports. Even though Sutter was notified by the FI prior to filing its CYE December 31, 1994 cost reports, it did not appear to fully implement the FI's recommendation until filing the CYE December 31, 1996 cost reports. For example, on its CYE December 31, 1996 cost reports, Sutter classified much less of its central supply costs to ancillary medical supplies (26 percent for Carmichael and 41 percent for Arden).

In addition, from a review of the current master list used by Sutter to classify each medical supply item as routine or ancillary, we noted that various routine medical supplies were classified as ancillary. A list of 68 routine items that we noted that were improperly classified as ancillary is included as Appendix A. The misclassification of routine items on Sutter's master list appears to have contributed significantly to the billing and cost errors discussed above. This list does not represent all items on Sutter's master list that may be incorrect. Sutter will need to review its master list to identify all improper classifications.

Under Medicare's rules (see pages 4 through 6 of this report), costs for items and services furnished routinely to all patients should always be considered as routine costs. In order to be classified as an ancillary cost, the item or service must be directly identifiable to an individual patient, furnished at the direction of a physician because of special medical needs, and be

either not reusable, represent a cost for each preparation, or be complex medical equipment.

The billings and costs we identified were for supplies that did not meet the specific requirements for treatment as ancillary medical supplies. As a result, Sutter may have been overpaid by Medicare. We did not quantify the impact of the unallowable billings or misclassified costs as our review was limited to determining whether supplies were billed as ancillary or claimed as ancillary costs that should not have been.

The improper billings and cost classifications occurred because Sutter had not adequately maintained its master list (including the current version used at the time of our review) that classified each medical supply item as routine or ancillary according to Medicare's rules. The incorrectly classified accounts occurred because Sutter had not followed its written procedures that required it to take into account any problems identified by its FI in the prior years' Medicare audits. Sutter's accounting staff said that, instead, they treated these accounts consistent with the cost reports they prepared in prior periods. They believed at the time that their method was appropriate and would not result in overpayments from Medicare. Sutter's staff also said that due to the sudden death of the employee responsible for preparation of the CYE December 31, 1994 cost reports, the reports in the following year had to be completed by other employees.

Recommendations

We recommend that Blue Cross ensure that Sutter:

- ▶ Reviews its master list of medical supplies to identify and correct all of its classifications of routine medical supplies that are classified as ancillary,
- ▶ Does not bill future routine items as ancillary or claim routine costs as ancillary, and
- ▶ Provides training to its staff to ensure that accounts are accurately classified and takes steps to ensure that its written procedures are consistently followed.

Sutter's Comments

Sutter concurred with our recommendations. It listed corrective actions that it has already taken and said that it will work with the FI to resolve the issues we identified in our audit. It also

Page 11 - Ms. Jacqueline Anderson

suggested that we rephrase certain statements made in the draft report. We considered their comments and made appropriate changes.

In addition, Sutter stated that it had not had an opportunity to review specific audit findings for items billed as ancillary supplies. Sutter's written response is attached as Appendix B.

OIG's Comment

We reviewed our findings with Sutter's staff at several meetings during the audit. However, in response to Sutter's comments that it had not had an opportunity to review the findings related to its billings, we met again with Sutter's staff and provided them an opportunity to review each beneficiary billing we questioned. We also left with them a list of the billings we reviewed.

Mutual's Comments

In its response to our draft, Mutual listed the actions it has planned to deal with our recommendations pertaining to periods before January 1, 1998. Mutual noted that it will not be able to conduct a review of current claims because Sutter elected to change its FI to Blue Cross. Mutual's written response is attached as Appendix C.

Blue Cross' Comments

Blue Cross verbally concurred with the recommendations in our draft that related to periods after January 1, 1998.

Final determination as to actions taken on all matters reported will be made by the HHS action official named below. We request that you respond to the HHS action official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination. To facilitate identification, please refer to the common identification number A-09-98-00073 in all correspondence relating to this report.

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In accordance with the principles of the Freedom of Information Act (Public Law 90-23), Office of Inspector General, Office of Audit Services. reports issued to the Department's grantees and contractors are made available, if requested, to members of the

Page 12 - Ms. Jacqueline Anderson

press and general public to the extent that the information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

Sincerely yours,

A handwritten signature in black ink, appearing to read "Lawrence Frelot". The signature is fluid and cursive, with the first name "Lawrence" written in a larger, more prominent script than the last name "Frelot".

Lawrence Frelot
Regional Inspector General
for Audit Services

Direct Reply to HHS Action Official:

Allysson Blake
Associate Regional Administrator for Medicare
Health Care Financing Administration
75 Hawthorne Street, 5th Floor
San Francisco, California 94105-3901

APPENDICES

List of Additional Routine Items That We Noted That Were
Classified on Sutter's Current Master List as Ancillary

Aid for short toilet	Nepro can formula
Aid for sock, flex rehab.	Offset spoon-OT
Aid for sock, molded	One way straw
Aid for sock, pull-rehab.	Overhead rod
Applicators	Pad, Geo mattress
Betadine	Pen, felt tip black-OT
Blue medium cushion	Posey deluxe gel cushion
Bronze cane-OT (occupational therapy)	Reacher easy grab
Brush, cleaning	Reacher easy grab-OT
Brush, denture	Reacher feather lite
Brush, foot	Reacher leather lite
Cushion, wheelchair	Reacher reg. for rehab.
Cushion, wheelchair gel	Reacher super lite
Diabetisource	Red liners (waste can liners)
Elevators, 6" foot spiral	Ring zipper pull
Enema bucket	Seizure (bite) stick
Enema oil	Shoehorn EZ
Enema, disposable	Shoehorn-OT
Enteral pump rental	Shoehorn EZ slide
Feeding cup-OT	Shoelace elastic black
Formula fiber	Sip-a-cup-OT
Formula Isosource	Soft pink cushion
Formula Osmolite	Spoon, Melaware
Formula resource diabetic	Spoon, soup weighted
Hid button hook	Stick, dressing deluxe
High side dish-OT	Suba seal mug-OT
Holder, utensil	Teaspoon, caltery grip
Hydrogen peroxide	Terrycloth mesh bath mitt
Impact w/fiber	Traction frame bed
Insulated mug w/lid-OT	Tray wheelchair arm
Isosource	Washmitt, quad med
Knife, rocker/handle	Water mattress
Lip plate-OT	Wheelchair, foam arm tray
Nail clipper board	Wheelchair, "L" bracket



Sutter Health

January 26, 1998

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BY TELECOPY AND U.S. MAIL

Mr. Lawrence Frelot
Regional Inspector General for Audit Services
Office of Inspector General
Department of Health and Human Services
Office of Audit Services, Region IX
50 United Nations Plaza
San Francisco, California 94102

Re: Draft Report of Audit of Sutter Health's Billings for Ancillary
Medical Supplies, OIG ID. No. A-09-97-00075

Dear Mr. Frelot:

Thank you for your letter dated December 22, 1997, and the opportunity to comment on the OIG's Draft Report of Sutter Oaks-Arden and Sutter Oaks-Carmichael Skilled Nursing Facility Billings and Costs for Ancillary Medical Supplies for 1994 and 1995. This letter and its attachment constitute our response to the draft report.

Nonconcurrence with Factual Matters

We have the following comments on the factual representations in the draft report. .

1. We have not had the opportunity to review the specific audit findings set forth in the draft report concerning Sutter Oaks-Carmichael's ("Sutter Health's") bills for ancillary supplies. Accordingly, we are not able to concur or nonconcur with those findings. In any event, you note in the draft report that the audit sample of these items was a "judgment sample" only and was not statistically valid.

2. On page two of the draft report it states that "[Sutter Health's accounting staff] believed at the time that their method would not result in unreasonable reimbursement from Medicare." We believe this would be more accurate if it stated that "They believed at the time that their method was appropriate and would not result in overpayments from Medicare."

3. On page two of the draft report it states that "Sutter staff also said that the cost reports for CYE 1994 were prepared by new employees without benefit of written procedures designed to avoid such classification errors." We believe this would be more accurate if it stated that "Sutter Health's staff also said that due to the sudden death of the employee responsible for preparation of the CYE 1994 cost reports, the reports had to be completed by other employees." For additional details of these events, please see my letter to Mr. Douglas Leonard dated November 14, 1997, a copy of which is attached "For the reasons stated in my November 14, 1997 letter, we believe it would be more accurate to delete the phrase "without benefit of written procedures designed to avoid such classification errors" from this sentence.

4. On page three of the draft report it states Sutter "owned six nursing facilities" at the time of the audit. This would be more accurate to state that one Sutter Health affiliate owned four nursing facilities (three freestandings and one distinct part) and a second affiliate owned another distinct part skilled nursing facility.

5. On page ten of the draft report, the language referred to in paragraph number two above is repeated. We request that it be revised as set forth above.

6. On page ten of the draft report, the language referred to in paragraph number three above is repeated. We request that it be revised as set forth above.

Corrective Actions Taken

We have the following responses to the recommendations contained in the draft report.

1. Charge Description Master Review

Recommendation: That Sutter review its master list of medical supplies to identify and correct all of its classifications of routine medical supplies that are classified as ancillary.

Action Taken: The routine items erroneously classified as ancillary on the Charge Description Master have been reclassified or are in the process of being reclassified as routine charges and that process is expected to be completed by June, 1998.

* Office of Audit Services Note — The letter attached to Sutter's response has been omitted because it pertained to issues that have been resolved.

2. Determine Fiscal Impact of Errors Identified in Audit

Recommendation: That Sutter determine the fiscal impact for the incorrect billings, the misclassified costs claimed for routine medical supplies, and the incorrectly treated routine supply accounts.

Action taken: The fiscal impact of these errors was not determined in your audit and, as your report has only recently been made available to us, has not yet been determined. Sutter Health will work with the fiscal intermediary to promptly quantify and resolve the issue of any overpayments made as a result of the errors identified in the draft report.

3. Refund for Any Overpayments in 1994-95

Recommendation: That Sutter make an appropriate refund, if necessary, to Medicare for the period of January 1, 1994 through December 31, 1995.

Action Taken: As stated above, Sutter Health will work with the fiscal intermediary to promptly quantify and resolve the issue of any overpayments made as a result of the errors identified in the draft report. Refund of any overpayments will be made promptly following resolution of that issue.

4. Audit CYE 1996 Cost Reports

Recommendation: That Sutter determine that its cost reports for Sutter Oaks-Arden for CYE 1996 accurately reflected proper billings and costs claimed for ancillary medical supplies and make an appropriate refund to Medicare, if necessary.

Action Taken: Sutter Health will work with the fiscal intermediary to resolve the issue of whether any errors identified in the draft report were repeated with respect to these CYE 1996 cost reports. Refund of any overpayments will be made promptly following resolution of that issue.

5. Future Conduct

Recommendation: That Sutter not bill future routine items as ancillary or claim routine costs as ancillary.

Action Taken: Sutter Health concurs in this recommendation.

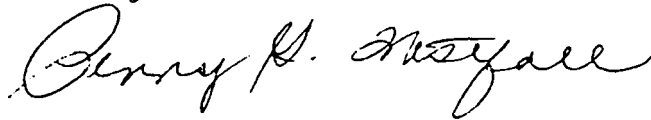
6. Training of Personnel

Recommendation: That Sutter develop procedures and provide training to its staff to ensure that accounts are accurately classified.

Action Taken: Sutter Health is in the process of augmenting the content of its training provided under its previously existing compliance program to give special emphasis to proper billing procedures for routine and ancillary supplies. This process will be completed by 1998.

Please do not hesitate to contact me if you have any questions concerning our response. Thank you.

Sincerely,



PENNY G. WESTFALL
Assistant General Counsel

PGW/lr
Enclosure

cc: Christie Hunting
Sheryl Vacca
Russell Hayman
Paul DeMuro

Office of Audit Services Note — The above noted enclosure has been removed because it pertained to issues that have been resolved.



Contractor for
MEDICARE

February 9, 1998

Mr. Lawrence Frelot
Regional Inspector General
Audit Services
Department HHS/OIG/OA
50 United Nations Plaza
San Francisco, CA 94102

RE: CIN: A-09-97-00075
Sutter Health

Dear Mr. Frelot:

We are in receipt of your December 22, 1997, letter and draft report on your review of ancillary medical supply costs claimed by Sutter Health during their cost reporting years December 31, 1994 and December 31, 1995. We welcome the opportunity to review the draft report and provide comments on the findings and recommendations included in the report.

We will be issuing Notice of Reopenings to Sutter Health concerning Sutter Oaks-- Arden, Provider No 05-5855 and Sutter Oaks - Carmichael, Provider No. 05-6304 to address the medical supply costs issue. We will be reopening their fiscal years ending December 31, 1994 and December 31, 1995, and fiscal period ending May 31, 1996, cost reports.

We will scope the medical supply costs during our review of the fiscal period ending December 31, 1996 cost reports. We will not limit this review just to Arden and Carmichael but, will also include Alzheimers, Provider No. 55-5400. We are not aware of a facility known as Amador.

We will work with Sutter Health on their filing of the fiscal year 1997 cost reports to ensure that medical supply costs have been properly accounted for in all of their facilities serviced by Mutual. We will review this area during our tentative settlement and desk review process of the cost reports.

Sutter Health elected on January 1, 1998 to have all of their facilities serviced by Blue Cross of California. The three facilities we were servicing have switched to Blue Cross. We will not be able to conduct a review of current claims.

We will keep you apprised of our activity on this issue. Please contact me at 402-351-2096, if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Charles Potter", with a long horizontal flourish extending to the right.

Charles Potter
Supervisor
Benefits Integrity Cost Report Unit

cc: Diana Townsend - HCFA Kansas City
Scott Manning
Liz Powers
Patty Aguilera
Shelly Foxworthy
Paul Hula